Trade Policy and Regional Integration: Implications for the Relations between Europe and Africa

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1. INTRODUCTION

THE linkages between trade policy and regional integration can be seen in two ways, depending on which is seen as the instrument and which as the objective. The 1980s have seen a revival of interest in regional integration schemes[1] and in virtually all the schemes adopted or considered in Africa,[2] coordination of trade policies (e.g. in the form of customs union) is seen as a means of achieving regional economic integration. In this paper we begin by taking this objective as given and comparing different forms of trade policy (unilateral, discriminatory multilateral and non-discriminatory multilateral). We then consider the other possibility, i.e. seeing regional cooperation as a means of achieving (or sustaining) a change in trade policy.

When trade policy is used specifically with a view to promoting regional integration then this is a particular instance of collusive trade policy. The collusion has the objective of reciprocal discrimination: country A favours B

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[1] See the June 1992 special issue of the *Journal of Common Market Studies*, Anderson and Blackhurst (1993) and de Melo and Panagariya (1993).

[2] Jebuni (1993) surveys the experience with regional integration in Africa and provides evidence on intra-regional trade.

against non-member countries C in return for B favouring A against C. Collusive trade policy need not take a discriminatory form. In the non-discriminatory alternative A and B agree to reduce their trade barriers not only against each other but also against C. The former type of collusion is used in customs unions, the latter in the GATT (now the WTO) where a concession granted to one country has to be extended to all. The use of trade policy for regional integration is not just a particular instance of collusive trade policy, it is also a particular form of reciprocal discrimination: the countries which are regional neighbours are likely to be similar in economic endowments. This is, of course, not inevitable: NAFTA is an example of a regional arrangement involving countries with very dissimilar endowments. However, regional integration in Africa (unless it involves South Africa or if a group of African economies were to form a customs union with a part of 'the North') typically involves members with rather similar endowments and therefore limited trade with each other.[3]

Thus, for regional integration to be the appropriate objective for trade policy, three steps need to be established. First, collusive trade policy must be superior to unilateral trade policy. Secondly, reciprocal discrimination must be superior to recriprocal non-discrimination. Thirdly, regional reciprocal discrimination must be superior to South–North reciprocal discrimination.

In this paper we first consider these three questions in turn: assuming that an African government was free to choose between these different types of trade policy, which would have most to offer? We then investigate whether the choices are interrelated: by choosing one now, does that make other options easier or more difficult now or later? In particular, is regional reciprocal discrimination a stepping stone or a stumbling block towards freer trade with the North?

2. THE IMPORTANCE OF TRADE POLICY REFORM TO AFRICA

Many African countries have had highly restricted trade. Usually restrictions have taken the form of foreign exchange rationing or import bans. Trade policy has commonly been used as a macroeconomic policy instrument, liberalised and tightened according to the balance of payments position. Hence, restrictions have not only been on average severe, but have also been volatile. The resort to trade restrictions was an important contributing factor to poor African economic performance. Easterly and Levine (1994) show that trade restrictions (measured by the black market premium for foreign exchange) were the single most powerful policy-induced cause of why Africa grew less rapidly than East Asia over the period 1965–90. Directly, trade restrictions so measured accounted for a per capita growth difference of 0.64 percentage points per annum, but

[3] This may, again, be contrasted with the case of NAFTA: 80 per cent of Mexico's exports are already destined for the US or Canada.

additionally, they found evidence of an effect via neighbouring countries. Where a group of neighbouring countries all adopt high trade restrictions the negative growth effect is reinforced by the factor 2.2. Thus, a regionally coordinated (though not regionally preferential) trade liberalisation would on their estimate have raised the growth rate by 1.4 percentage points.

In the past decade many African countries have liberalised trade as the centrepiece of wide-ranging reform programmes. For example, Zimbabwe, Kenya, Uganda and Ghana now have convertible currencies for current (and in some cases also for capital) transactions, and have largely eliminated quantitative restrictions. Parallel to these trade reforms marketing and financial institutions have been reformed, creating an environment in which trade reform can translate into resource reallocation. However, trade liberalisation attempts have often not been sustained. For example, the Nigerian liberalisation of 1986 was gradually eroded before being completely abandoned in 1993. Even in those countries where reforms have been sustained for some time there are often reasonable grounds for doubting their continuance. For example, the Ghanaian government is thought to have come close to reimposing a fixed and appreciated exchange rate early in 1994. Limited policy credibility is harmful since it deters fixed investment: potential investors will prefer to remain liquid while it is unclear as to which sector will be favoured by trade policy (Dixit, 1989). this might be one of the reasons why, despite liberalisation and generous tax incentives, Africa is currently attracting only a negligible proportion of the foreign direct investment into developing countries (see Miller and Sumlinski, 1994). A recent survey of attitudes to investment in Africa of European companies concludes that 'political and economic stability is the primary concern of the offshore private sector' (Blakey, 1992, p. 15).

Hence, while the first point has argued that trade restrictions are costly, the second suggest that unconvincing liberalisation is also costly. Evidently what is needed is liberalisation with lock-in. This is particularly important since lock-in of trade reform can help to lock in other liberalisations. This has been one of the advantages suggested for NAFTA. A convincing trade liberalisation creates an export sector which constitutes a lobby for maintaining reforms. To conclude, trade policy is of importance for African economic performance, but even where wide-ranging liberalisations have been implemented, African governments have been unable to convince potential investors of the strength of their commitment to the new policies.

3. THE CASE FOR AFRICAN TRADE POLICY TO BE MADE UNILATERALLY

Does the trade policy of an African country gain from being coordinated with that of other countries, or is it sufficient to set policy unilaterally? Unless there are some substantial and clear gains from coordination then unilateral policy is much to be preferred: as the Uruguay Round has made abundantly clear, international coordination of any decision is costly, slow and fraught with pitfalls of misunderstanding.

Additional costs arise because it is not sufficient to coordinate trade policy: almost always compensation schemes will have to be set up. It is, at least in principle, possible to devise a customs union which is Pareto-efficient in the sense that it is welfare improving for the union in aggregate while the rest of the world is not made worse off.[4] However, in general some members of the union will lose while others gain. Obviously, the gainers can compensate the losers, but compensation causes difficulties (how are welfare gains and losses to be established in practice?) and easily leads to tensions between the members.

Given the cost of coordination and compensation, in some sense the 'default' is to leave decisions at the national level. The case for African trade policy to be set with a view to promoting regional integration is a special case of this more general question, whether any form of collusion in trade policy (other than to exploit monopoly power) is necessary or desirable. Economists since Adam Smith have pointed out that collusion is not necessary: trade liberalisation need not be reciprocated to be welfare improving. Nevertheless, the mercantilist position of viewing trade liberalisation as a zero-sum game has powerful appeal in international trade negotiations. Hudec (1987) has brilliantly described the history of the GATT (where mercantilist thought is reflected in the terminology of 'concessions') in these terms: each country sees the liberalisation of its own trade policy as a cost rather than a benefit and will therefore require 'compensation'.

This view was not limited to the rich countries. In describing the early history of the GATT Hudec draws attention to the fact that the developing countries, including African countries, most strongly felt that they could not benefit from unilateral liberalisation. By wrongly conceiving trade liberalisation as something which needed to be collusive, African governments tended to see national trade liberalisation as the 'price' which might have to be paid for the gain which was in the form of the trade liberalisations of other countries. Having conceptualised trade liberalisation in this way, the natural next step was then for African governments to lobby for the 'gain' without the 'cost'. They therefore pressed through UNCTAD for other countries to make non-reciprocated trade concessions to African countries. This was conceded since at the same time the

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4 The mental experiment involved in establishing this is simple. Trade flows between the three countries are frozen. Then the customs union between A and B is formed. This results in a real income gain for the union members and hence an increase in their demand for imports from C. The external tariff is then raised to keep those imports at their pre-union level. With tariffs at this level there then is a gain for the union and no loss for the outside world. See Kemp and Wan (1976).

rich countries came to see preferential trade arrangements for developing countries as an appropriate instrument for promoting development, partly on the basis of infant industry arguments.[5] Thus, the true gains from trade liberalisation, which could have been achieved by an African government unilaterally reducing its trade barriers, were not realised because of the misplaced context of collusion and bargaining in which trade policy was located.

While it is mistaken to see collusion as necessary, it might still be desirable: it is obviously possible for a country to gain more from, say, a customs union than from unilateral liberalisation. But while the Kemp-Wan result establishes that it is possible to design a customs union in such a way that it is net trade creating, it is not at all unlikely that in practice unions will be trade diverting, a point stressed by Bhagwati. Free trade areas (FTAs) are permitted under current GATT rules only if 'duties and other regulations of commerce' are set by the FTA members in such a way that they are not 'higher or more restrictive' for non-members than was the case in the pre-FTA situation'.[6] It has therefore been argued that GATT rules should be revised so that FTA members will be required to form a customs union (i.e. to adopt a common external tariff) and that the tariff should be set no higher than the minimum of the members' pre-union tariff rates. As Bhagwati points out, even such new rules would not be sufficient to prevent trade diversion. This is because the new instruments of protection, in particular voluntary exports restraints and anti-dumping actions, are much more difficult to police than tariffs.

Suppose countries A and B form a union and A is more efficient in the production of good 1 than country B. The union will then lead to trade creation exports of good 1 from A to B. Producers of good 1 in country B may then be tempted to offset the growing market share of A (which they cannot resist since A is a fellow member of the union) by trying to reduce the market share of country C. That is they will try to reduce imports from outside the union, e.g. by bringing an anti-dumping action. If C were more efficient than A in the production of good 1 and B's lobbying producers would succeed in keeping imports of good 1 (from all sources) into B constant then there would be a net loss: imports into B from C would have been replaced by imports from the less efficient producers in A. As long as protection takes forms which are difficult to police, regional integration may well lead to trade diversion in this way. For NAFTA it has been suggested that both American and Mexican producers will attempt to bring actions against imports from third countries. Also, the EU has liberally used both VERs and anti-dumping actions against Asian textile producers.

There is therefore a presumption that a regional FTA will become trade diverting. But even if this does not happen, the scope for a welfare improvement

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[5] These preferences are now seen as of very limited value, see e.g. Langhammer (1992).

[6] *The Economist* (27 June 1992, p. 73) and Bhagwati (1993).

through an FTA of neighbours is very limited, because, as noted above, in Africa countries are very similarly endowed. Indeed, there is quite a strong case to be made for why unilateral trade policy is all that an African government needs to bother with: it will achieve virtually all of the enormous gains which would accrue to Africa from global free trade (Husain, 1993). This position is not to be dismissed lightly: at present, Africa's exports are largely free of import duties and so in the short term it has little to gain from reciprocated over unilateral trade liberalisation.

African economies are usually 'small' in the sense that they cannot influence their terms of trade, and by the mid-1980s usually had highly restricted trade which it is reasonable to regard as very costly. The appropriate policy was to dismantle these barriers and negotiation was at best irrelevant and at the likely worse would involve long delays. In terms of Viner's two-goods, three-countries world, the extreme case (in which negotiation would be irrelevant) would arise if two African countries would both import good 1 from the third country, the rest of the world, and export good 2 to it. Formation of a customs union would then not change trade patterns at all and the African countries would clearly not gain anything from the union. This might well be a realistic description of some of the existing African integration schemes: they might simply be vacuous (cf. de Melo et al., 1993; and Foroutan, 1993). A notable exception is SACU (which has operated since 1910) in which South Africa ensures dissimilarity.

Further, unilateral, non-preferential trade liberalisation will enhance regional integration without actively promoting it. As governments recognise the rationale for unilateral trade liberalisation, regional integration is increased as a by-product, since trade barriers are reduced against neighbours as part of the general reduction in trade barriers. For example, if both Kenya and Tanzania have convertible currencies and few quantitative restrictions on international trade, then they will trade more with each other. As Young (1993) stresses, the rise of intra-region trade in East Asia has very much occurred in this form: as the by-product of unilateral trade liberalisations.

However, the Husain and Hudec position overstates the case against an African government having some interest in the trade policies of other countries and so having an interest in collusive trade policy. This is because the analysis is (in the tradition of Viner) limited to trade creation and trade diversion effects.

4. AFRICA'S INTEREST IN NON-DISCRIMINATORY COLLUSIVE TRADE POLICY

Although few of Africa's current exports encounter trade barriers, this is to ignore the gains from removing restrictions on goods which Africa does not currently export but could do were access easier. Because African governments have sought non-reciprocated trade concessions, developed country governments have felt free to withhold access in key areas such as non-traditional agricultural produce. As Bhagwati (1993) emphasises, the GATT is the main institutional hope of peripheral countries not in the large blocs. The periphery has the strongest interest in making the GATT process work. An implication is that African governments should be cheering for global collusion, and so supporting GATT to the hilt. The danger that the continental trade blocs will frustrate the GATT must be taken seriously. However, African attitudes to the GATT can make only a marginal contribution to whether it succeeds or fails. Hence, encouraging global collusion should not be a policy to which African governments commit significant negotiating resources.

Also, Africa's interest in the success of the GATT is not entirely unambiguous. Textile restrictions on East Asian exports to Europe under the Multi-Fibre Arrangement have actually benefited Africa, by protecting African textile exporters to Europe from East Asian competition. This component of African manufactured exports is thus currently contingent upon the maintenance of a unilateral preferential trade policy on the part of Europe. This also applies to some agricultural exports. For example, Mauritius benefits from the European common agricultural policy, being allowed to sell part of its sugar exports at the high intra-EU price. A successful GATT would substantially lower the sugar price received by Mauritius (while at the same time removing the quantitative restriction to which its exports are subject).[7]

5. AFRICA'S PRESENT RELATIONS WITH EUROPE

At present the trade relations between European and African countries are not characterised by reciprocity. African exports enjoy preferential treatment in the EU under the Lomé convention but this relationship is asymmetrical. African countries are under no obligation to let in imports from EU countries. Conversely, when an African government agrees (under donor pressure) to liberalise its import restrictions, it does not thereby gain improved access to the markets of European (or any other developed) countries.

The preferential tariff treatment of Africa has been eroded by the gradual lowering of tariffs applicable to competing developing countries. Further, the Convention is not as generous as it may appear because while Africa's traditional exports can typically enter the European market free of restrictions, temperate agricultural products are restricted due to the Common Agricultural Policy (CAP) and exports of textiles and clothing are restrained under the Multi-

[7] Exports exceeding a given quota come in at the world price rather than at the higher EU price. See Woldekidan (1992).

Fibre Arrangement (MFA). Access of African countries to the European market is thereby hampered and this matters to those countries which are able to move beyond their traditional specialisation such as Kenya and Zimbabwe. The conclusion of the Uruguay Round will improve access by phasing out the MFA and reducing trade restrictions related to the CAP. However, in both cases this will take time.

Although the present Convention is due to run until the year 2000, a mid-term negotiation process is currently under way. This renegotiation is not a formality: 'Lomé's poor record makes it ripe for reappraisal' (Bossuyt et al., 1993, p. 5). It is therefore timely to consider a fundamental reconstruction of the trade relations between Africa and Europe based upon reciprocity.

6. AFRICA'S INTEREST IN AFRICA-NORTH RECIPROCAL DISCRIMINATION

We now consider reciprocal trade discrimination between an African country and a developed country or trading bloc such as the European Community. It is, perhaps, noteworthy that the predominant current collusive trade negotiation in Latin America is North – South, whereas for Africa it is intra-African. NAFTA has been negotiated as a deal between Mexico and North America, but it is envisaged by Latin American governments that this would provide the template agreement by which a free trade zone could be expanded to other Latin American countries. The African negotiations have, by contrast, linked the PTA with southern Africa. Here we consider the Latin American model.

The first powerful argument in favour of reciprocal discriminatory trade liberalisation with the North is that it might achieve virtually all of the gains which Africa would realise under global free trade while being much more within African negotiating reach. As Srinivasan (1993) shows in a critique of Krugman (1993), free trade within a trading bloc can achieve for its members all the gains of global free trade if the composition of the bloc spans the global range of production.

Potentially, Africa might negotiate with any of the big three trading blocs, NAFTA, the EU or Japan. Politically, each has some claims to feasibility. US trade policy is to a considerable extent determined by ethnic lobbies, hence the bilateral deals first with Israel and now with Mexico. It is not inconceivable that the Afro-American lobby could push through an equivalent bilateral deal with an African government or group of countries. Japan, unlike the EU and NAFTA, is not a trading bloc, and so might conceivably be more amenable to negotiation. However, evidently the most plausible negotiating partner is the European Union since this is the bloc with which Africa does most of its trade and has the strongest diplomatic ties. Free trade with the EU would be tantamount to global free trade from Africa's viewpoint. While GATT-based global free trade would offer a little more (although as discussed above it would open Africa up to competition from East Asia in Northern markets). Africa is (as noted above) not able to exert major influence on whether GATT succeeds in liberalising world trade, whereas it is, perhaps, able to negotiate a reciprocal deal with the EU. Hence joining a trade bloc with Europe would be no worse than what Africa could achieve from global liberalisation while it would be easier to achieve.

The second, and arguably most important argument in favour of reciprocity with a part of the North is that it can enhance the credibility of African trade liberalisation. As discussed in Collier, Greenaway and Gunning (1993), unilateral African trade liberalisations have encountered and are likely to encounter major problems with respect to credibility. Lack of credibility played a major role in the abortive Kenyan trade liberalisation attempts in the 1980s and after a failed reform future credibility becomes more difficulty to achieve.

The simplest credibility problem arises if there has been no political change so that the government proposing to dismantle trade restrictions cannot be seen as clearly different from the regime which introduced the restrictions.[8] In addition, donor pressure (particularly if accompanied by aid-for-reform packages, as is common in SAPs) will make it less likely that the reform will be sustained.[9] Donor support introduces the possibility of time inconsistency: a government which commits itself to trade liberalisation only because of the aid offered, will reverse its policy once the aid runs out.

Lack of credibility is costly even if the perceptions of private agents are mistaken and the liberalisation is in fact sustained. For if (unlilateral) liberalisation is seen as being unlikely to persist, then there will be little investment in the export sector and hence little supply response. African governments therefore need a device for locking themselves in to a newly liberalised trade policy in order to signal to private agents that the new policy will persist. Participation in a regional scheme can provide such a signal.

This is because reciprocal trade discrimination is not just an agreement for each country to liberalise trade; its essential feature is that it is a reciprocated threat. If A were to reimpose trade restrictions on B, then B would reimpose restrictions on A. Because A is now subject to these threats, which would not be there were A's liberalisation unilateral, A faces higher costs of reimposing restrictions. This will help to lock in reform: lobbying pressure for a reversal of trade liberalisation is more likely to be resisted the higher the cost of reversal. In addition, when liberalisation is reciprocal there will not only be pressure against, but also lobbying in support of reform. (This is the political economy argument for the

8 This appears to have been an important determinant of the success of recent Latin American trade liberalisations. Alam and Rajapatirana (1993) stress that in all 16 countries which they survey there was a change in the political regime which helped to start or to reinforce the reforms.

9 See Rodrik (1989), Collier and Gunning (1992 and 1993) and Gunning (1994).

'mercantilist' approach of the GATT: reciprocity induces exporting firms to lobby in favour of trade liberalisation of their own country since they realise that this is necessary to get access to foreign markets.) Hence, A's liberalisation is more credible to the private agents in its economy. As a result, they are more likely to make irreversible commitments such as investing in the export sector. Reciprocal discrimination thus provides a means by which the government can bind itself. The same argument applies to developed countries. When Spain and Portugal joined the EU they considered a key advantage 'the enhanced credibility that commitment to the EC lent their proposed changes in economic regime. If other means of establishing credibility were available, accession would lose some of its charm.' (Winters, 1993, pp. 109, 116).

This is the key aspect of NAFTA: it is not important primarily because it provides Mexico with access to the North American market, but because it considerably increases the probability that Mexico will retain its current, unilaterally adopted, liberal trade policies, and therefore reduces the risk involved in investing in the export sector. Post-NAFTA, an investor in the Mexican manufacturing sector exporting to the North will face a much more secure future than an investor in the African manufacturing sector exporting to the North. At present, the attempt to enhance policy credibility is through donor conditionality: aid is promised in return for reforms. All governments face the problem that their sovereign power to renege on commitments is a liability, and so seek devices for restraining themselves by passing on sovereignty to some other agency in specific spheres of policy. Donors are, however, implausible 'agencies of restraint' because they are neither plausible nor participatory (Collier, 1991). Worse, by not imposing penalties when agreed reforms were abandoned, they have reinforced the time inconsistency problem generated by their own support for reform thereby weakening the credibility of future liberalisations.

Most non-African governments have chosen to restrain their sovereign power over trade policy by the creation of multi-national threat-making agencies in which they participate both as threat makers and as threat receivers. African governments are unusual in not having taken part in this process. But they do find themselves now threat receivers from donors in a non-reciprocal and therefore unacceptable political relationship.

Regional integration changes the relationship between a government and the private sector. As the influence of any individual faction is diluted regional policy making may be welfare improving. In the example of de Melo et al. trade policy is determined in a game between the government and a lobbying faction. The government is unable to precommit itself and the lobby moves first, thereby endogenously determining the parameters of that part of the government's objective function which is not strictly economic. In deciding on its lobbying activity the lobby takes the optimal response of the government into account, that is it acts as a Stackelberg leader. In this model welfare, as perceived by the government, is reduced as a result of its reacting to pressure.[10]

Suppose regional integration involves two such countries and that integration implies that trade policy must be identical. The national lobbies remain active as before and since their demands are not identical the regional institution setting trade policy is assumed to respond to an average of the demands of the two lobbies. In addition, government preferences on trade policy (other than in reaction to lobbying) differ and, again, the regional decision is based on an average. De Melo et al. show that in this simple model regional integration reduces lobbying pressure and thereby leads to an outcome with less government intervention. This is the 'preference-dilution' effect: since the regional institution is less responsive to an individual lobby than the national government was, lobbying becomes less effective. Recall that the lobbyists are Stackelberg leaders: they take the institution's reaction into account in deciding on the extent of their lobbying activity. With the marginal benefits reduced through preference-dilution, the optimal levels falls: each country will experience a reduction in lobbying.[11]

But this result is not sufficient to establish in what direction integration will affect trade policy, except if the governments' own preferences are identical. For in that case preference dilution is the only effect which need to be considered and the sign of that effect is unambiguous: intervention will be reduced. However, if government preferences do differ there is an additional effect to consider: the 'preference-asymmetry effect'. The two countries will have to compromise; the less interventionist country will have to allow an increase in intervention while the other country will agree to a reduction in intervention (compared to its pre-integration national policy). Hence the effect necessarily works in opposite directions in the two countries. Conceivably, it could dominate the preference-dilution effect in the less interventionist country so that integration makes trade policy in that country (and only in that country) more rather than less restrictive.

Clearly, the more similar governments are in their policy preferences, the weaker the asymmetry effect. If, abstracting from lobbying influences, African countries joining a regional scheme are in agreement on the objectives of trade policy, then only the preference-dilution effect need to be considered and integration will help trade liberalisation.

Note that while the trade theoretical literature indicates that similar countries are unsuitable customs union members (except possibly at income levels where trade in differentiated products becomes important) the preference-dilution

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[10] The additional cost involved in the rent-seeking activities themselves is ignored.

[11] Note that collusion of lobbyists is ruled out. In European terms: French and German farmers cannot jointly lobby the Commission on the treatment of the common agricultural policy in the GATT. This restriction is important and probably unrealistic. For example, European auto manufacturers have formed an EC-wide lobby to keep out Japanese imports. Cf. Bhagwati (1993).

argument points the other way: the effect is stronger (since preference-asymmetry is weaker) the more similar the countries are (not in terms of endowments or trade patterns but in terms of preferences).

The preference-dilution effect as modelled by de Melo et al. is not entirely convincing. It is not explained why the government cannot resist the lobby or influence the outcome by precommitting itself to a trade policy (i.e. effectively changing the order in which the two players move). Nor does the model explain what the government would lose by leaving the regional arrangement. It appears that the only benefit it would thereby forego would be the preference-dilution effect itself. But then no credible threat is involved so that it is not clear why the lobby would no longer be able to achieve under integration what it could achieve before. It is not enough to answer that this is precluded by the need to reach a compromise with the union partners: there must be a penalty for leaving the union. If the union is to dominate unilateral trade reform then this penalty must consist of the loss of a benefit which cannot be realised unilaterally.

Hence the proposed arrangement of a reciprocal European-African customs union would work if the access to the European market which it would guarantee would be better than what a country could achieve in an individual reciprocal arrangement. This condition is very weak. The real choice seems to be between unilateral, unreciprocated liberalisation and liberalisation within the context of a reciprocal North – South arrangement. It seems inconceivable that any individual African country would be able to negotiate improved access to the EU market. But as a member of a regional bloc a country would lose access if it violated the rules of the bloc and this amounts to a convincing penalty on policy reversal.

Thirdly, as discussed above, Africa's current access to Europe is dependent upon the unilateral preferential trade policy which Europe has adopted with respect to Africa, and this preference might be regarded as precarious because it is not in the long term self-interested. If it is a good idea for A to have liberal trade against B, without B reciprocating, then why is it not also a good idea for A to have liberal trade against C without C reciprocating? In the case of European imports of textiles, the domestic political imperative from the textile producer lobby was protection against the Far East. The act of unilateral preference for African producers lined up African governments (and the domestic aid lobby) in favour of the Multi-Fibre Arrangement, leaving the East Asian exporters diplomatically isolated. However, because this discrimination by the North in favour of Africa is unilateral, African governments have little control over whether it is maintained. African investors must therefore be wary of a change in the Arrangement which could reduce their preferential access. This is particularly important because it is the drift of thinking about European Union trade relations with developing countries. The new study by Grilli (1993) argues that EU trade relations have over-emphasised Africa whereas the future trading interest lies with Asia and Latin America. As Kanbur (1993) argues in his review of Grilli's book, this line of analysis augurs very badly for Africa: if the EU loses interest in Africa then Africa would lose both its present favoured access to its major market and the scope for reciprocal trade deals. Indeed, without an offer of reciprocity developed countries might restrict access to their markets other than for Africa's traditional exports.

This is essentially a defensive argument for joining a bloc. The benefit expected is not so much an improvement in market access as preventing a deterioration in access. This same defensive motive for regionalism applies to developed countries. Baldwin (1993, p. 396) points out:

> Many developing and small industrial countries want to participate in regional integration agreements with the United States and the Community because of their belief that this will result in a more limited use of US and EU anti-dumping and countervailing-duty laws.

This defensive motive appears to be the main reason for the eagerness of the EFTA countries to enter into an association accord with the EU.

This argument has gained force in the 1980s, partly because of the difficulty of concluding the Uruguay Round and also because of the increased reliance of protectionists on NTBs which clearly are more difficult to police than tariffs. Dornbusch et al. (1989) consider this important for access of developing countries to the American market:

> . . . the increasing interference with trade by application of the US trade laws raises the costs of and uncertainty of exporting to the US market. Individual developing countries would therefore find it of interest to strike a bargain where unimpeded access to the US market is the *quid pro quo* for a privileged opening to the US of their own markets.[12]

Fourth, so far we have implicitly assumed that if unilateral trade liberalisation is as good as, or better than, collusive trade liberalisation, then it is politically easier than collusive policy: with a unilateral policy the government does not have to worry about negotiations with another government. The greater political ease of unilateral policy is not necessarily a reasonable assumption. A government will be faced by domestic lobbies in favour of protection and these might be able to block unilateral liberalisation yet not block collusive liberalisation. Collusive liberalisation will be politically easier if the population at large makes the same conceptual error that Hudec attributes to African governments: that is, if it sees the national reduction in protection as the 'price' to be paid for foreign reductions in protection. This may be an easier policy to 'sell' politically than the message that unilateral trade liberalisation raises domestic real income, because trade restrictions are often not recognised as internal transfer policies. Indeed, the irony in the history of the GATT is that it has been successful probably precisely because it has proceeded in mercentilist terms, i.e. by swapping concessions. A policy maker convinced of the intellectual case for unilateral liberalisation might therefore still favour a reciprocal arrangement: it makes it easier for him to convince his domestic opponents.

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[12] Dornbusch, Krugman and Park (1989, p. 36), as quoted by Hindley and Messerlin (1993).

Thus, it may be easier for an African government to get trade liberalisation accepted against the domestic protectionist lobbies if it can argue that this is the price to be paid for better access to European markets. This is approximately how the world achieved free trade in the nineteenth century. Irwin (1993) provides a revealing historical account of collusive trade liberalisation. He shows that in the nineteenth century, the process which achieved the global freeing of trade was bilateral trade deals, with the benefits spread by means of conditional most favoured nation clauses: any deal which A made with B was open for C to demand the same deal with A. He shows that the initiating bilateral deal between Britain and France cumulated through the use of the conditional MFN clause to cover the world trading system. France had little directly to gain from reciprocated unilateral trade liberalisation. Yet by making its liberalisation reciprocal the government could win over domestic opinion which would have blocked unilateral action. Small-group collusions were in this instance the stepping stones to free trade whereas unilateral liberalisations might have been blocked by domestic lobbies.

Fifthly, such an arrangement may be used to 'import' institutional arrangements considered desirable by the union's members. Again, this has played a role in the negotiations on the European Economic Area (EAA) between the EU and the EFTA-countries. The EFTA-countries by acceding to the EEA accepted EU commercial law, in particular anti-trust law (and they even agreed to abide by EU interpretations) (Hindley and Messerlin, 1993). Collusive trade policy naturally leads to a coordination of other policies. Rather than devising all institutions for the regional association from scratch, an association with the EU might make it possible to 'import' institutions deemed useful, on a menu basis.

In summary, 'regionalism' need not be based on the belief (in the case of Africa very likely mistaken) that there are net welfare gains (in terms of trade creation effects dominating trade diversion) to be realised in a regional customs union which cannot be attained through unilateral trade liberalisation. A regional customs union tied to a northern market would dominate unilateral liberalisation in five ways: it would achieve as much as Africa can expect to gain from global liberalisation; it would establish credibility of trade reform; it would serve a defensive purpose, avoiding that Africa would be left out in a world of trade blocs with GATT rules insufficiently enforced; it might be politically easier to achieve than unilateral reform; and, finally, it might facilitate the adoption of useful institutions by the regional union.

7. AFRICA'S INTEREST IN REGIONAL RECIPROCAL DISCRIMINATION

African regional integration has long held a certain romantic appeal. It is again fashionable, partly because of '1992' in Europe and NAFTA in North America.

However, as noted above, NAFTA is decidedly not the same thing as African regional reciprocal trade discrimination since it is a North–South deal.

Foroutan (1993) reviews the seven major African schemes for regional integration which have to date advanced further than the drawing board. She demonstrates that in practice even these schemes have barely been implemented, nor have they had a discernible effect on trade flows: African economies trade very little with each other and the share of such trade in their total trade is no higher than prior to the launch of the schemes. She explains this in part by drawing on the results of Foroutan and Pritchett (1992). Since African national factor endowments are similar, and per capita incomes too low for trade in differentiated products to be substantial, there is little scope for intra-African trade. A gravity model of trade finds that intra-African trade is no less than is appropriate for its economic structure. This implies that even were governments successful in negotiating and implementing regional trade liberalisation, little extra trade would take place.

Worse, what is intended as a regional trade liberalisation may actually make trade policy more restrictive. This appears to have happened in Zimbabwe where quotas which carried no restrictions on the country of origin have partly been replaced by quotas for imports from PTA members. Firms covered in a recent industrial survey (June 1993) reported that they had been unable to import from non-PTA countries as a result of this.

Husain (1993) qualifies the conclusion that little extra trade would be generated, arguing that official figures greatly understate intra-African trade because they omit smuggling. However, this is less convincing a critique than might appear. Paradoxically, much of the present unofficial intra-African trade is the direct consequence of a failure of regional policy coordination. The lack of fiscal harmonisation has created artificial incentives to trade. The remarkable petroleum subsidies in Nigeria have given rise to smuggled exports to neighbouring countries, while the far higher taxation of cocoa in Ghana than in the Côte d'Ivoire induced cocoa smuggling. Regional integration would remove the basis for this trade. Hence, one of the sound arguments for African regional coordination of trade policies is that it would reduce this sort of trade. It is precisely because African governments still rely heavily upon a narrow range of commodity taxes, such as beer and cigarettes, which if taxed at different rates in neighbouring countries can easily be smuggled, that regional coordination of economic policies is most desirable.

As this example implies, regional integration is a broader concept than trade policy. Even if the countries in a region trade freely with each other, they may not be integrated. Several policies beyond trade policy will influence integration and may benefit from being coordinated. To take some obvious ones, transport policy may benefit from coordination either from shared airline services or a common rail and road system. Energy policy may benefit from being coordinated if water is used for hydro-electric power. Fiscal policy may benefit from being coordinated as harmonised tax rates reduce smuggling. Additionally, as Bliss (1993) argues, if African governments continue to compete for foreign investment by offering tax holidays, they will get worse terms than if they adopt a common incentive structure. That is, collectively, Africa might be 'large' in the niche market for certain types of foreign direct investment. There are probably much stronger arguments for the purely regional coordination of fiscal, monetary and infrastructure policies than for trade policy.

8. IS THERE A TRADE-OFF BETWEEN DIFFERENT TRADE POLICIES?

Regional reciprocal trade liberalisation can be either complementary with or an alternative to non-preferential liberalisation. In one sense they are clearly alternatives: if all trade restrictions are removed non-preferentially and unilaterally then there is no room left for reciprocal discrimination. In another sense they are clearly complementary: if all trade restrictions are removed non-preferentially then this at the same time removes the impediments to regional trade.

However, there are also more subtle interrelationships. One theme in the literature is the interaction of regional reciprocity, of which the EU is the most important, and near-global reciprocity as exemplified by the GATT. This is a central focus of de Melo and Panagariya (1993). The emphasis is, however, not on a two-way interaction but rather on the consequences of regionalism for globalism. One argument is that regional integration reduces the number of players in the GATT bargaining game, thereby reducing the free rider problem, and so making GATT bargaining, based on the most-favoured nation clause, more feasible. On this view, the formation of regional groups would be a necessary stage on the road to global freeing of trade. However, the majority view at present is that this is likely to be negative. For example, Krugman and Bhagwati are both hostile to the perceived trend towards three continental trading blocs, essentially seeing them as reducing the incentives for multilateral trade liberalisation while increasing the incentives for protectionism within the bloc. While this is a depressing conclusion as far as Africa is concerned, it is not one which African governments can do much about. The pertinent policy question within Africa is not globalism versus regionalism but unilateral liberalisation or Africa-North reciprocal discrimination versus regional reciprocal discrimination.

Above we have argued that the form of collusive trade policy which is most pertinent to Africa is North–South reciprocal discrimination along the lines of NAFTA. However, NAFTA is a negotiation in which only one (important) Latin American country is currently involved. If, as expected, NAFTA expands, it will do so piecemeal. This piecemeal sequential expansion is not really a feasible model for Africa. Africa has more than twice as many countries as Latin America, and has no natural first negotiator equivalent to Mexico. For negotiating purposes with the European Union, Africa needs supra-national entities. At one extreme Africa could wait until there is a functioning Pan-African Common Market. However, on Foroutan's argument above, it might have to wait a long time. The alternative is the creation of regional trading groups of countries in the context of North – South trade liberalisation. For example, the PTA, but preferably a much smaller grouping, would negotiate with the EU for reciprocal freeing of trade.

This could be a small group of nations submitting themselves to a participatory supranational agency, following the model of the Franc Zone. Supranational control implies a loss of sovereignty. In the rules vs. discretion literature this is, of course, seen as advantage. Nevertheless governments are naturally loath to bind themselves. However, given the extent of donor pressure sovereignty in the field of trade policy is somewhat illusory. The combination of donor power and absence of penalties lands African countries in the worst of possible worlds: reform is resented because it is imposed by outsiders and it is difficult to sustain because reversal carries no penalties. If this is to be avoided then donor conditionality must be replaced by something like the proposed voluntary associations.

The two monetary unions which make up the Franc Zone each have a central bank which is governed by the member countries (not by France). This institutional arrangement implies a relatively effective form of external discipline: a country which violates the rules can be expelled (by its fellow member countries) and it would thereby lose the advantages of convertibility and of automatic temporary financing of budget deficits. Hence the Franc Zone, unlike donor conditionality as currently practised, relies on a convincing penalty.

While the Franc Zone has in the past only focused upon monetary unions, its key elements (participatory supranational control and convincing penalties) can be applied to customs unions. Indeed, currently, the Zone is being transformed to include trade relations. Both the West and Central African Monetary Unions have been reconstituted as Economic and Monetary Unions. Hence, the existing institutions of European-African reciprocity are venturing into trade relations at just the time when the traditionally non-reciprocal Lomé Convention governing trading relations is being formally reappraised. The EU could offer association accords (similar to the arrangements already in effect with EFTA constituting the European Economic Area) to groups of countries which set up customs unions under supranational control of the participating African countries. Additionally or alternatively, the regional trade groupings which now exist in Africa could apply to the EU for association accords. The review of the Lomé Convention provides an opportunity for both parties to create the framework which would invite such initiatives by African regional groups. Thus, the review of the

Convention does not need suddenly to abandon non-reciprocity, but rather to add the possibility of reciprocity. Such an addition would to an extent counteract the diminution of the non-reciprocal preferences which has occurred through global liberalisation. Association would imply reciprocal free trade, i.e. the two markets, the EU and the African group would form a customs union. Such a set-up has three advantages.

First, the arrangement is entirely voluntary. The EU would make an offer on a take-it-or-leave-it basis: there would be no pressure on African countries to accept the offer. Such an optional arrangement is likely to be more viable than the agreements associated with donor conditionality.[13]

Secondly, self-government makes reform more acceptable and therefore more likely to be sustainable. Discipline is not imposed by an external agency such as the IMF or the World Bank (both of which are in Africa perceived as alien institutions, see Collier, 1991) but by a self-governing regional group. An important corollary is that if this form of regional cooperation is to work effectively, the number of members has to be small. While there is a tendency to aim for the expansion of existing African regional integration schemes into continent-wide organisations, this is likely to make an institution which has to rely on self-imposed discipline ineffective.

Finally, it would achieve credibility. For if a government were to restore trade restrictions it would not only lose the free access to the rest of the customs union but also the access to the EU which is tied to union membership. That access is valuable because the present preferential access is by no means unrestricted. African exporters enjoy GSP and ACP tariff preferences but these are subject to quantitative limits. Successful exporters of products considered 'sensitive' (e.g. agricultural products) by the EU face quotas or 'voluntary' export restraints. For example, voluntary export restraints were used against Mauritius when its exports of knitwear started growing rapidly. As Winters (1993) points out, 'the fact that rapidly growing trade flows could, and have been, constrained greatly reduces the incentive for suppliers to establish effective export channels'.

Although some African nations could join the European trading bloc piecemeal, regional negotiations would serve to increase African bargaining power. Further, recall that Irwin's analysis of nineteenth century liberalisation showed that the agreement between Britain and France served as a template which other governments could choose to replicate. Similarly, in Africa, not all governments would at the same time want to join a reciprocal trade arrangement

[13] A country may, of course, decide that the political costs of abandoning protection are prohibitive so that it chooses not to participate. But then such a country would have been an unwilling participant in trade liberalisation under a SAP. Hence the fact that the reciprocal arrangement is voluntary does not make trade reform attempts more likely than under a SAP, but it does make it more likely that if trade is liberalised the reforms will be sustained.

with the North, but ideally an institutional form should be designed in which it is possible eventually to include the whole of Africa without that requiring 50 bilateral negotiations between the EU and each African entrant. Given the pace of EU negotiations, and the periodic halt on entry imposed by the EU for reasons of internal negotiation, a more streamlined process is needed, incorporating the same openness as the British-French trade liberalisation of the nineteenth century. This could be achieved if the membership of an African customs union linked to the EU could be expanded without having to reopen negotiations: a potential new member would negotiate entry into the union only with the existing members. By joining it would automatically gain access to the EU market and reciprocate by removing restrictions on imports from the EU.

If trade liberalisation with the North is achieved through reciprocal discrimination with Europe rather than either through the GATT or through unilateral African trade liberalisation, then the relationship between trade liberalisation with the North and African regional integration is thus complementary. Liberalisation with the North reinforces the regional trade liberalisation. By contrast, if liberalisation with the North is either through GATT or through unilateral African trade liberalisation, then there is some danger that these can be in conflict with trade policies which promote regional integration. Trade barriers are maintained against the North in order to leave room to grant preferences to neighbours.

However, this is not inevitable. One way in which unilateral trade liberalisation and regional integration-promoting trade policies are compatible is if reciprocity within the region is used as a device for creating threats which act as a deterrent to the abandonment of unilateral policies. For example, in Latin America there has been a scramble to negotiate regional trade agreements not so much in order to achieve regional free trade, but in order for governments to demonstrate that they wish to maintain newly liberalised trade by creating penalties for themselves in the form of threats from neighbouring countries. This is an appropriate policy, because it is relatively easy to negotiate: governments are creating at the regional level the agencies of restraint which can then bind national policy. They participate both as threat receivers and as threat makers. While this is useful, in the African context it is probably insufficient as a device for restraining national policy because, with so little of Africa's trade being intra-regional, the cumulative threats are rather weak. Supplementing regional integration with reciprocal discrimination with part of the North strengthens the threat.

The above argument has been that regional integration and unilateral trade liberalisation can be complementary in that regional integration strengthens unilateral liberalisation through its threat-making capacity. There is also a good case for arguing that the complementarity works in the other direction: unilateral trade liberalisation makes regional integration-promoting trade policy more feasible. Foroutan (1993) argues that non-discriminatory liberalisation is a necessary prelude to regionally discriminatory liberalisation.[14] She explains the past failure of regionalism at least in part by the highly protectionist trade policies which most African governments have adopted. Until these barriers are reduced, the transfers generated by regional reciprocity are too powerful to be politically sustainable. With highly protected industries which governments wish to retain, regional liberalisation creates large transfers of industries and revenues. The attempt to mitigate these effects by compensation schemes is too complex to be workable. Further, where the compensation schemes are implemented they introduce substantial distortions. Regional reciprocal discrimination starting from a position of high levels of protection creates very powerful redistributions between countries, while the overall net gains from liberalisation are small or even negative because such a small proportion of trade is intra-African. This can be contrasted with Europe, where protection levels are much lower so that intra-European redistributions are much smaller, whereas a much larger proportion of Europe's trade is intrinsically intra-European, so that the gains from freeing trade are large. Europe is an effective reciprocal trade discrimination agreement politically because it achieves large gains in allocative efficiency with small redistribution effects. African regional groups have the opposite characteristics: small (or negative) allocative efficiency effects with large redistributions. An implication of this argument is that only once African governments have substantially liberalised their trade non-preferentially will the conditions be created which would permit regional trade integration to be politically feasible. Hence, a phase of mutual but non-discriminatory liberalisation, which might as well be unilateral, is a necessary precursor to sub-regional reciprocity.

9. THE EUROPEAN INTEREST

Africa might, as we have suggested, have much to gain from a reciprocal trade agreement with Europe, and yet be denied the opportunity because Europe perceives no benefits from such a scheme. Indeed, as Grilli (1993) argues, the traditional concern of Europe with Africa has not been deeply rooted in European self-interest and is likely to be replaced with an Asian focus. Here we discuss the potential benefits to Europe of a reciprocal arrangement.

Africa is not a major market for Europe. However, Europe holds a wholly disproportionate share in Africa's imports. Africa's very poor economic performance over the past twenty years has consequently been costly for European exporters. If Africa had approached East Asian growth rates over the past two decades it would now be a sizeable market. Europe therefore has much

[14] It should be noted that Mexico had unilaterally liberalised its trade policy *before* the NAFTA negotiations.

the greatest interest outside Africa in improved African economic performance and hence in sustainable policy reform. Conversely, precisely because Africa is currently economically small and has a negligible manufacturing sector, trade liberalisation cannot be seen as politically costly: unlike Eastern Europe, Africa is not currently in a position to disrupt European markets with its exports.

Europe has an interest in African policy reform over and above its own commercial interest. All European Union members, individually and collectively, have substantial aid programmes in Africa and these have been used increasingly to induce policy reform. In addition they are major contributors to the multilateral agencies and thereby indirectly finance 'structural adjustment' programmes. The efficacy of these expenditures has increasingly been called into question within Europe. Whereas in the past aid was to an extent seen as a pure donation, it is now often cast as a means of achieving the objective of policy reform. The presence of a sizeable aid programme therefore demonstrates Europe's perceived interest in African economic performance, while the modest achievements to date demonstrate the limitations of the adopted approach (see World Bank, 1994). Reciprocity might constitute a policy instrument which is both more powerful and less costly.

In addition the European Union has shown an interest in new regional integration initiatives in Africa. In the present phase of the Lomé Convention the promotion of regional integration receives special emphasis and indeed more than 10 per cent of the total budget has been allocated for this purpose. Currently the Commission is promoting the 'Cross Border Initiative', aimed at establishing a common external tariff and reciprocal trade arrangements between participating African regional groupings. The European Commission quite reasonably sees itself as having a natural institutional comparative advantage in promoting regional cooperation.

The above arguments suggest that Europe has interests in African economic success and that it recognises these interests. However, arguably the most potent reason for Europe to be concerned with African economic policy is that it fears the consequences of continued African economic failure. The vision of a 21st century Africa immiserised and politically unstable, generating an exodus of migrants and providing a base for international crime, has already been widely canvassed (Kaplin, 1994).

10. CONCLUSION

In Africa trade liberalisation in the context of discriminatory regional schemes such as customs unions has been pursued as a means of promoting regional economic integration. Its scope in this role is limited since African countries are insufficiently dissimilar. Indeed, such schemes may not only be costly (in terms of the difficulties involved in coordination and compensation) but in terms of trade creation entirely 'vacuous' (de Melo et al., 1993) or, worse, they may well be trade diverting. In many African countries there is enormous scope for efficiency gains through the removal of import controls, but this does not require reciprocity. Whatever benefits can be realised in this way are better attained through unilateral reform. Regional integration is then likely to follow as a by-product of unilateral liberalisation, as has happened in East Asia.

There are two counters to this. First, unilateral trade liberalisation in Africa has not been very successful, partly as a result of donor involvement. Secondly, and relatedly, if the objectives are not limited to the efficiency gains of customs union theory, then regional collusion in trade policy may still dominate unilateral liberalisation, in spite of the problem of endowment similarity.

Unilateral liberalisation would be dominated by reciprocal free trade between an individual African country and the European Community. Indeed, it is unlikely that global liberalisation would offer more (and African countries have not been able to influence the outcome of the GATT negotiations anyway). Most importantly, reciprocal free trade with the North would establish credibility of trade reform by introducing convincing penalties on policy reversal: it would involve secure access to the EU market (a result which might be much more difficult to achieve if an individual country negotiates with the EU) and the loss of this access would present a credible threat.

We have suggested that the Franc Zone monetary unions offer a model for tying small, self-governing groups of African countries in an FTA to the European Union. A policy debate has started on the future of Lomé.[15] This might be a useful institutional framework for linking Africa with Europe with reciprocal trade policy replacing the present unreciprocated preferential arrangement.

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[15] Van der Linden (1993, p. 87) suggests that the interest expressed by South Africa in joining Lomé offers an opportunity to reconsider the nature of the present Convention, replacing unreciprocated preferential treatment by the arrangement we have proposed. Renegotiation of Lomé could be a first step towards a trade agreement between Europe and Africa based on reciprocity.

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